BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Petitions of TICOR TITLE INSURANCE COMPANY, TICOR TITLE INSURANCE COMPANY OF CAL., FIRST AMERICAN TITLE INSURANCE COMPANY, *for Redetermination Under the Insurance Tax Law*

Appearances:

For Ticor Title Insurance:	Ms. Maureen McGuirl Mr. Norman Barker Attorneys at Law
For First American Title Insurance:	Mr. Harry G. Melkonian Mr. Chris Rudd Attorneys at Law
For Department of Insurance:	Mr. Hon Chan Senior Staff Counsel
For Board of Equalization:	Mr. Monte Williams Administrator
	Mr. Gary J. Jugum Assistant Chief Counsel
	Mr. David H. Levine Senior Staff Counsel

MEMORANDUM OPINION

The Board heard these petitions on June 23, 1993 in Sacramento, California. The petitions concern the proper measure of tax imposed on title insurers in California.

Section 28 of Article XIII of the California Constitution imposes a tax on title insurers measured by all income on their business done in this state, with exceptions not relevant here. These provisions are codified at Revenue and Taxation Code sections 12202 and 12231. The question before the Board is what constitutes all income of a title insurer.

FACTS

There are two basic elements of a title insurance policy issued in California: a title search to discover defects, if any, in the title; and a policy of insurance which insures against the existence of any defects in the title that were not disclosed in the title search. Both these elements may be performed by the insurer. The measure of tax with respect to such policies is not at issue here. However, in California it is more common for an ‘‘underwritten title company’’ (UTC) to perform the title search element of the title

insurance policy, and to issue the title insurance policy as the agent of the title insurer. It is the title insurer's income from such policies issued by UTCs on behalf of the title insurer that is at issue here.

Title insurers often conduct business in this state pursuant to underwriting agreements with title companies. The title company may be wholly or partly owned by the title insurer, or its ownership may be completely independent of the title insurer. A title company that has an underwriting agreement with a title insurer is called an underwritten title company. The underwriting agreement authorizes the UTC to issue a policy of title insurance as the agent of and in the name of its principal, the title insurer. The UTC performs a title search and issues a preliminary title report that shows the defects, if any, to the title. The UTC then issues a title insurance policy, as agent of and in the name of its principal, and receives the premium for that policy.[1] For its services, the UTC retains an amount set forth in the underwriting agreement, generally about 90 percent of the total premium.

Petitioners have not reported as taxable income amounts retained by the UTCs. The Department of Insurance (Department) recommended that the Board issue, and the Board did issue, deficiency assessments measured by such amounts for tax year 1987. Petitioners filed timely petitions for redetermination.

BACKGROUND

The manner of providing title searches and title insurance has evolved in California over the past 100 years into the current arrangement. During that time, there was a shifting of the manner of providing title insurance from the title insurer performing the title searches and providing the insurance policies to today's more common method at issue here. Prior to 1942, title insurers were taxed on the same basis as other insurers, gross premiums. In 1942, a constitutional amendment was adopted which changed the basis of tax on title insurers from gross premiums to all income.

In 1953, the California Supreme Court decided the case of *Groves* v. *City of Los Angeles* 40 Cal.2d 751, which involved a measure of tax based on gross premiums. In *Groves*, the insurer issued its insurance, bail bonds, through its agents, bail bondsmen. In the cases before us, the UTC typically performed the title search element of the title insurance policy. In *Groves* the bail bondsman performs no analogous service or function. A person purchasing a bond paid the bail bondsman, who retained 90 percent of the premium and remitted the remaining 10 percent to the insurer. The Court held that the 90 percent retained by the bail bondsman was part of the insurance premium and was taxable to the insurer. This case is the primary basis for the Department's conclusion that the amounts retained by the UTC are part of the title insurance premium and are therefore income to the title insurer, and taxable as such.

[1] A single fee must be charged for the title insurance policy, which includes the title search, without a separate statement of the charges related to the title search. (Ins. Code § 12401.1.)

After the 1942 constitutional amendment, title insurers reported tax measured by the entire title insurance premium when the title insurer performed the title search and provided the insurance. However, when a UTC performed the title search and issued the policy of insurance as the insurer's agent, the title insurer reported tax measured only by the amounts transmitted to it from the UTC. The title insurers have been reporting tax in this manner for 50 years. Notwithstanding the *Groves* decision on which the Department relies, neither the State Board of Equalization nor the Department have adopted any regulations requiring that the amounts in question be included in the measure of tax. Likewise, the Department has not taken any other action contrary to the title insurers' method of reporting tax until its recommendations for the assessments at issue here. In fact, during this period the Department of Insurance issued written statements supporting the interpretation now urged by the Petitioners.

The most recent authority with regard to taxation of title insurance companies is the California Supreme Court's decision in *Title Insurance Company* v. *State Board of Equalization*, 4 Cal.4th 715 (1992). In *Title Ins. Co.*, the Court found that the ''title insurer and the title company, through the underwriting agreement, have agreed to allocate the labor, risk, liability and premium'' associated with the title insurance contact. (*Title Ins. Co.*, at 725.) Further, the Court found that the ''title insurer forgoes the portion of the premium attributable to the risk that is allocated to the underwritten title company.'' (Ibid.) The Court held that title insurers may not be taxed on claims paid by underwritten title companies pursuant to underwriting agreements between the two.

ANALYSIS

Petitioners argue that the UTC is not an agent of the title insurance company for purposes of calculating the ''all income'' measure of tax under California's Insurance Tax Law. In response, the Department argues that the UTC is, in fact, the title insurer's agent for purposes of accepting not only that portion of the premium remitted to the title insurer, but rather the entire amount paid by the customer. Petitioners argue that the 1942 amendment to the constitution did not intend to increase the title insurers' tax liability by a factor of ten. The Department points out that the decision that forms the basis for regarding amounts retained by an insurer's agent as part of the insurer's gross premiums was issued more than ten years after the 1942 amendment, which means that neither title insurers nor other insurers knew what the Supreme Court would ultimately decide on that issue. Petitioners argue that *Groves* was a case solely on the issue of what constitutes ''gross premiums'' and the Department responds that it is also relevant to the question of what constitutes ''all income.''

We agree with the Court's analysis in *Title Ins. Co.* that the title insurer and the underwritten title company have divided the labor, risk, liability, and premium and that by doing so, the title insurer forgoes the premium retained by the title company. Therefore, the premium retained by the UTC should not be included in the measure of ''all income'' of the title insurance company.

Further, we find that the Court's decision in *Groves* does not apply. We not that in *Groves* the basis for taxation was ''gross premiums'' not ''all income'' as required for title insurance companies. As previously stated, the UTC typically performed the title search element of the title insurance policy, unlike *Groves* where the bail bondsman performed no such equivalent activity.

In addition to these points, for almost 50 years the Department has taken no action on this issue, almost 40 of which were after the *Groves* decision. Petitioners argue that a change of course at this time must be based on some principled explanation, and we agree. At this juncture, after 50 years of acquiescence in the manner of reporting by petitioners, the Department has failed to establish that a different method of taxation is correct. The longest of long-standing administrative practice is entitled to great weight. Here the interpretation in practice was contemporaneous, continuous, and enduring. (See, generally, *Transamerica Occidental Life Ins. Co.* v. *State Board of Equalization* (1991) 232 Cal.App.3d 1048; *American Hospital Supply Corp.* v. *State Board of Equalization* (1985) 169 Cal.App.3d 1088.)

We therefore hold that the amounts retained by UTCs are not part of the all income measure of title insurers' insurance tax liability, and we order that the determinations be canceled.

Done at Sacramento, California this 5th day of January 1994, by the State Board of Equalization.

Brad Sherman, Chairman
Matthew K. Fong, Member
Ernest J. Dronenburg, Jr., Member
Attested by: Burton W. Oliver, Executive Director